

Message Text

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SUBJECT: ECONOMIC AND DEVELOPMENT REVIEW OF JAPAN

REF: PARIS 18200; TOKYO 9180

1. SUMMARY. EMBASSY AGREES WITH EDRC FORECAST OF RELATIVELY STRONG GNP GROWTH FOR JAPAN IN 1977 AND BELIEVES GOJ WILL TAKE FURTHER STEPS TO SUSTAIN GROWTH MOMENTUM INTO 1978. CURRENT ACCOUNT SURPLUS APPEARS UNAVOIDABLE SO LONG AS PRESENT IMPORT STRUCTURE REMAINS UNCHANGED. END SUMMARY.

2. AS OUTLINED REF (B), EMBASSY WOULD AGREE WITH EDRC REVIEW THAT JAPANESE ECONOMY WILL REGISTER RELATIVELY STRONG GROWTH OF AT LEAST 5.5 PERCENT IN CALENDAR 1977. WE CANNOT, HOWEVER, ACCEDE TO ASSUMPTION THAT GOJ WILL NOT SEEK A STIMULATORY SUPPLEMENTARY BUDGET IN AUTUMN 1977 TO SUSTAIN GROWTH INTO 1978. FACING UPPER HOUSE ELECTIONS ON JULY 10, PM FUKUDA IS ADHERING TO A PUBLIC LINE OF FISCAL RESPONSIBILITY, CITING A NECESSITY TO REDUCE THE BUDGETARY DEFICIT CURRENTLY RUNNING 30 PERCENT OF GENERAL
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ACCOUNT EXPENDITURES, AND DANGERS OF EXACERBATING 9.2 PERCENT INFLATION RATE. BUT THE RECORD SHOWS THAT SUPPLEMENTARY BUDGETS HAVE

BEEN INSTITUTED IN EACH OF THE PAST TEN YEARS. FURTHERMORE, A SUPPLEMENTAL BUDGET WAS ADOPTED LAST YEAR DESPITE A SIMILARLY LARGE BUDGETARY DEFICIT. WE NOTE THAT THE BUSINESS COMMUNITY HAS ALREADY PUBLICLY BEGUN TO AGITATE

FOR FURTHER FISCAL STIMULATION THIS FALL.

3. WHETHER A SUPPLEMENTAL BUDGET IS INTRODUCED MAY WELL DEPEND ON POLITICAL AS MUCH AS ECONOMIC FACTORS. IF LIBERAL DEMOCRATIC PARTY (LDP) SUFFERS MAJOR SETBACK IN UPPER HOUSE ELECTION, FOR EXAMPLE PM FUKUDA COULD COME UNDER PRESSURE TO RESIGN AND RESULTANT LEADERSHIP STRUGGLE COULD DELAY INITIATIVE ON A SUPPLEMENTAL. ON THE OTHER HAND, IF, AS IS MORE LIKELY, LDP LOSES ONLY MODERATELY, RECORD NUMBER OF BILLS PASSING DIET DURING THIS LAST SUMMER AUGERS WELL FOR INTER-PARTY COOPERATION. EMBASSY BELIEVES THAT IF ECONOMIC SIGNS CLEARLY POINT TO NEED FOR SUPPLEMENTAL, OPPOSITION PARTIES CAN BE EXPECTED TO COOPERATE IN PASSING

A SUBSTANTIVE SUPPLEMENTAL BUDGET, ALBEIT AFTER EXTRACTING THEIR OWN PRICE.

4. AS EDRC REPORT NOTES, CONSUMER DEMAND HAS REMAINED FAIRLY STEADY AND PROSPECTS ARE GOOD FOR FURTHER STRENGTHENING. FOR PRESENT, AND FOR MEDIUM-TERM, CENTRAL AND KNOTTIEST PROBLEM IS SLUGGISH INVESTMENT IN PLANT AND EQUIPMENT. EMBASSY BELIEVES IN WORDS OF EDRC REPORT "SORRY STATE OF BUSINESS CONFIDENCE" IS UNAVOIDABLE PSYCHOLOGICAL PRICE OF TRANSITION NOT ONLY FROM HIGH GROWTH TO LOWER GROWTH EXPECTATIONS BUT FROM ECONOMIC GROWTH FOCUSED ON MANUFACTURING TO ONE MORE HEAVILY LIMITED OFFICIAL USE

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DEPENDENT ON SERVICE INDUSTRIES. INTEREST RATES HAVE DECLINED STEADILY, AND FURTHER CUTS ARE SCHEDULED; HOWEVER, WHETHER THIS WILL HAVE DESIRED RESULTS IS OPEN TO QUESTION. WITH SEVERE OVERCAPACITY STILL COMMONPLACE IN BASIC INDUSTRY, EARLY STIMULUS FROM FURTHER INTEREST CUTS IS UNLIKELY. EMBASSY QUESTIONS WHETHER FURTHER INVESTMENT IN THESE INDUSTRIES IS EVEN ADVISABLE. EMBASSY WOULD ASK THE JAPANESE DELEGATION TO INDICATE WHAT MEASURES THE GOJ COULD TAKE TO STIMULATE PRIVATE INVESTMENT IN THOSE SECTORS FOR WHICH DOMESTIC DEMAND HAS BEEN RISING, AND IN OTHER INDUSTRIES WHERE PER CAPITA PRODUCTIVITY REMAINS RELATIVELY SLOW.

5. EMBASSY FULLY AGREES WITH EDRC FORECAST THAT GIVEN GOVERNMENT'S COMMITMENT TO ACHIEVING 6.7 PERCENT GNP GROWTH AND GROWTH COMPONENTS DURING RECOVERY AT THIS PACE, JAPAN WILL AGAIN GARNER LARGE CURRENT ACCOUNT SURPLUS IN 1977 AND ONLY SLIGHTLY SMALLER SURPLUS IN 1978. PRESENT IMPORT STRUCTURE WOULD INDICATE THAT EVEN IF PRIVATE INVESTMENT PICKS UP SIGNIFICANTLY, CURRENT ACCOUNT SURPLUS WILL PERSIST UNDER PRESENT IMPORT STRUCTURE. EMBASSY WOULD URGE JAPAN TO TAKE POSITIVE STEPS TO ENCOURAGE

THE IMPORTATION OF FINISHED GOODS AS A MEANS OF REDUCING
THE CURRENT ACCOUNT SURPLUS AND REDUCING INFLATION RATES.

6. EMBASSY DOES NOT FULLY SHARE SECRETARIAT'S OPTIMISM
WITH RESPECT TO OUTLOOK FOR CONSUMER PRICES. CPI
INCREASES HAVE CONTINUED AT BETTER THAN NINE PERCENT RATE
THROUGHOUT FIRST HALF OF THIS YEAR, WITH ONLY SMALL
PORTION OF THIS INCREASE ATTRIBUTABLE TO DELAYED INCREASES
IN REGULATED PRICES. ALTHOUGH WE ARE CONFIDENT THAT
GOJ WILL WORK TO ACHIEVE SUSTAINED GROWTH, FEARS OF
INFLATION COULD MODERATE THE SIZE OF ANY STIMULATIVE
PACKAGE THIS FALL.

7. FINALLY, EMBASSY WOULD POINT OUT TO JAPANESE DELEGATION
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THAT RELIANCE ON EXPORT INCOME TO STIMULATE DOMESTIC DEMAND
DOES NOT SEEM TO BE WORKING.
FURTHERMORE, THE SIZE AND COMPLEXITY OF THE JAPANESE
ECONOMY WOULD SEEM TO INDICATE THAT RELYING ON EXPORTS
AS A COUNTER-CYCLICAL MEASURE WILL HAVE INCREASINGLY LESS
EFFICACY IN THE FUTURE. WE WOULD QUESTION THE JAPANESE
DELEGATION MORE CLOSELY ABOUT JAPANESE INDUSTRIAL
RESTRUCTURING PLANS, ESPECIALLY WITH REGARD TO POLICIES
TOWARDS DIRECT INVESTMENT ABROAD.
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